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Total Onboarding

Synopsis: *Andes Wealth has brought back the investment policy statement generator—but that’s only a small part of what the program offers.*

Takeaways: *It’s possible to determine a prospect’s risk tolerance with one image. The IPS pulls from a full suite of client onboarding tools, and the program also offers a robust way to stress-test your model portfolios under different market conditions.*

About 15 years ago now, Joel Bruckenstein’s T3 conference featured an interesting series of presentations; people used various methodologies to quantify the returns vs. cost of some of the popular financial planning software packages then on the market. The surprising winner, with a thousand-plus percent return on investment (measured by, among other things, staff time savings), was IPS AdvisorPro, the program that auto-created investment policy statements for clients, rather than forcing you to craft them by hand.

No federal or state regulator requires you to have an IPS for retail clients. But for those who did, these documents helped keep clients from making emotional decisions during market downturns or when the U.S. market is outpacing diversified portfolios. (They can also be a decisive tool if you’re ever in a legal dispute with clients over your investment recommendations. More

on that in a minute.)

In 2013, the market’s return-on-investment champion was sold to Fidelity, which was acquired by Broadridge, and IPS AdvisorPro was subsequently taken off the market as an independent software package.

A variety of client onboarding tools each feed data into the final IPS document.

I bring this up because we may be entering another one of those periods when it would be helpful for clients to lock in their portfolio management policy. And also because a new—and I think better—investment policy statement generator has recently hit the market.

The product is part of a suite of tools available from Andes Wealth Technologies (<https://andeswealth.com>)—a company that offers its IPS

generator as part of a comprehensive client onboarding toolkit that is different from anything I’ve yet seen in the marketplace. It was created by Andes founder Helen Yang, who holds an MS in finance from MIT, where she worked with Andrew Lo, co-wrote some papers with Lo and along the way won the 2011 Harry M. Markowitz Award from the *Journal of Investment Management* for one of the co-written articles (along with co-author Eric Fielding).

As you’ll see in a moment, Yang’s mission in our advisor space is to give you practical and creative ways to apply historical return and volatility data with your clients and prospects. (Conflict alert: After I talked with Yang for this and another article, I agreed to serve on the company’s advisory board, and one of the company’s upgrade ideas was my suggestion. But I don’t receive any additional compensation if you decide (or not) to buy the software.)

Client onboarding tools

To understand the utility of the IPS generator, it helps to first understand Andes’ client onboarding tools, which all feed different kinds of data into the IPS document. Most people, if they’ve heard of Andes at all, probably think of it as a risk tolerance instrument in the same market as Riskalyze and FinaMetrica—although Andes uses

a very different methodology.

Your goal with any risk tolerance tool is to match an appropriate portfolio to the client's risk tolerance score—right? Andes handles this chore in the most direct possible way, by showing the client all the important information in one single picture. Taking the asset allocation of all your model portfolios, the program uses historical data to show the spectrum of possible returns out to an 80% confident rate for any given six month one year period. (See graphic, next page.)

This one-image risk tolerance instrument paints a picture of the tradeoffs involved in the prospects' portfolio choice. They see the spectrum of returns within a 80% confidence band for each portfolio, organized from least to most risky, left to right. The bond-heavy portfolios on the left have a narrower spectrum of possible returns (green for upside, red for downside) than the equity-heavy portfolios on the right.

Prospects can see each portfolio's maximum (to 1 1/2

standard deviations one-year downside and upside return in percentage and dollar terms. Then they select the model that they feel most comfortable with. A section on the right shows an asset breakdown of the portfolio they've selected.

That, believe it or not, is it; that is, you've just assessed the client's risk tolerance. It's hard to imagine a simpler—and more directly implementable—way to match clients with their appropriate portfolios. Elsewhere, I've wondered how advisors would defend some of

Click on the bar with the upside/downside tradeoff that you feel most comfortable with.



the other risk tolerance assessments in court if clients were to challenge the methodology. But here, when clients are shown the risk/return trade-offs using widely-accepted historical data, and then select their own portfolio—and especially if they then sign off on it in an IPS—that would appear to be the gold standard for defensibility in court.

Suppose you want to know more about your clients than just which portfolio they prefer? Andes offers a very short supplemental “risk appetite” quiz (sample question: *You are on a TV game show and can choose one of the following. Which would you take? A. \$1,000 in cash. B. A 50% chance at winning \$5,000. C. A 25% chance at winning \$14,000. D. A 5% chance at winning \$100,000.*) which is designed to serve as a check-and-balance on the initial instrument. If a client chooses

a right-side bar corresponding to an aggressive portfolio, but grades out as having a low risk appetite, then you might want to spend a little more time talking about the the desired investment mix.

Advisors can have their clients take, online, a few other 3-5 question quizzes, including: Investor Temperament (sample question: *How would you change your asset allocation if the S&P 500 declined 10% in the past six months and other asset classes performed as you expected?*); Loss Aversion, Herding (how much are you influenced by your friends and neighbors?); Overconfidence (Do you believe you can pick investments to beat the market?); a quick cognitive test; a quick Financial IQ test (*Suppose the interest rate on your savings account is 2% a year and inflation is 3% a year. After one year would the*

money in the account buy more or less compared to today?) Finally, a “Describe Yourself” test asks clients to select personality traits that fit them.

I was brave enough to take all the quizzes, and after about 15 minutes I got back a profile describing me to my advisor:

Your Investor Persona: Passive Investor.
Your Behavior Risk Index: 7
Investor Temperament: Passive
Loss Aversion: No
Overconfidence: No
Herding: No
Cognitive Ability Test: Very Good
Financial IQ: Excellent

Investment Policy Statement

The data from the risk tolerance assessment, including the portfolio the client selected and the results of any quizzes

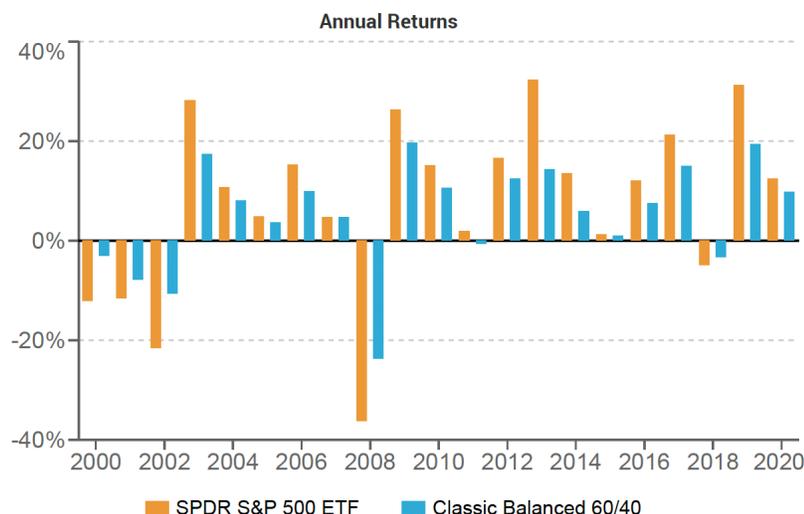
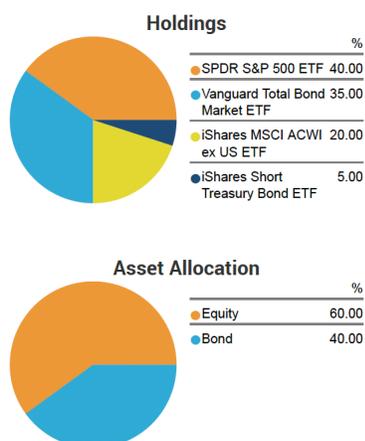
Asset Allocation

Investment Horizon: 5-10 years

Model/Strategy Name: Classic Balanced 60/40

Portfolio Composition:

This Classic Balanced Model Portfolio consists of 60% in stocks (including U.S. and intl. stocks) and 40% in fixed income (including bonds, short term and cash).



the prospect might have taken are automatically pulled into the client’s IPS document, along with the characteristics of the portfolio that the client selected. To create this document, you first take the client through a short on-screen worksheet, where the client gives you his/her primary investment goals, amounts and dates (\$120,000 by 9/1/2030 for education of two children in 9/1/2024; \$2 million by 6/30/2040 for retirement, etc.).

The IPS generator pulls all this data together into a customizable 5-page document, plus a cover page (white-labeled to your firm, with the clients’ names on it) and the final signature page. The text offers an explanation of the purpose of the IPS, a list of the investment objectives pulled from the worksheet, a graphic that reproduces the risk tolerance page where the client was invited to choose portfolios (with the selected portfolio highlighted), a pie chart of the asset allocation of that model portfolio, annual returns of that model portfolio or asset allocation going back 20 years, plus explanations of the financial advisor’s and clients’ duties and responsibilities while managing the portfolio. (See graphic, previous page.) There’s a graphic which shows how the range of expected returns tends to narrow over longer time periods, reinforcing the message that the best course is usually to stay the course.

The client reads it over and signs, and you have an IPS in the file without having to spend a lot of time on it. I’m not sure

how you would measure the return on investment, but I suspect that creating the same document from scratch would take hours.

Stress test tool

Interestingly, we’ve only covered about half of what Andes provides—but the other half can be described in a few sentences. Andes uses the same historical return and standard deviation data to map out the efficient frontier for any historical time period you might want to explore, and throws it up on a graph. You can see the efficient frontier over the last five years compared with the very different frontier for the 2008-9 markets. The program will also map the actual return and volatility of your model portfolios next to this efficient frontier for any of these time periods.

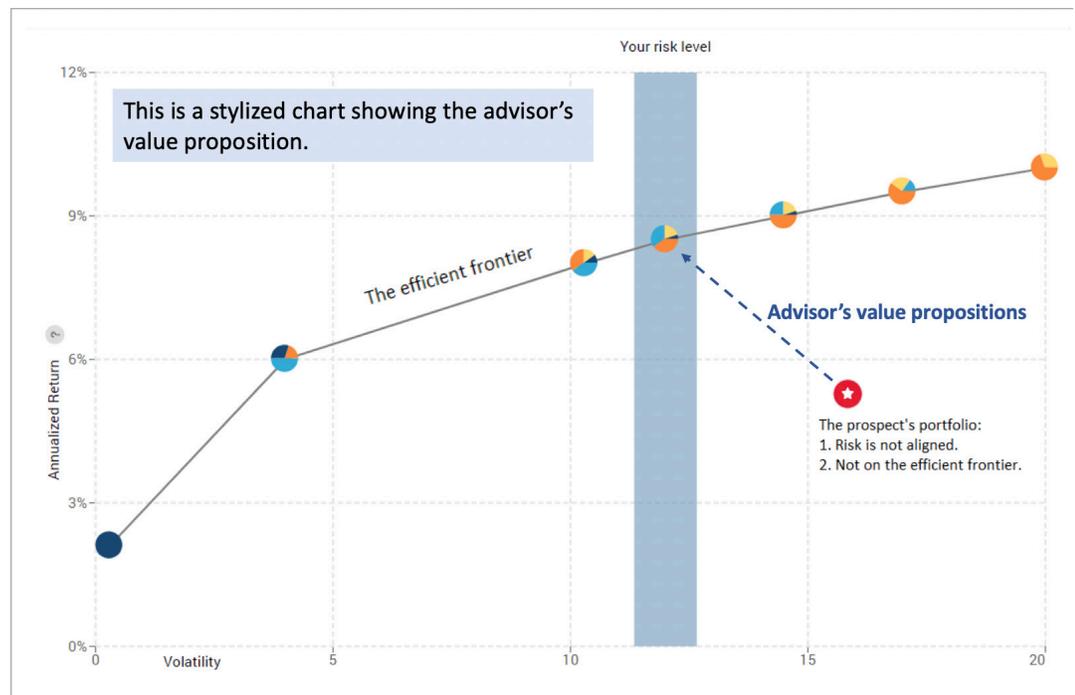
Why would you want something like that? This feature

lets you go back in time and stress-test your model portfolios under different market conditions. It also lets you show clients how the portfolio they chose will perform when the bulls are running hard or the markets are bearish. (Some advisors include a conversation like this at the start of the investment relationship.)

You can also show the client’s existing portfolio over each of these time periods, and there’s a colored vertical band which corresponds to the client’s risk level from the risk tolerance test. (see graphic). In one simple graph, the client can see two things: that her existing portfolio is far from efficient, and that it is also far from the appropriate risk tolerance band. (See graphic, below.)

Of course, the model portfolio she chose is right there in the band where it belongs—because it was selected to be so.

For existing clients, the



program will map actual returns vs. the efficient frontier that would be expected based on historical data. Why would you want something like that? When clients are worried that the market is in a downdraft; you can show that the portfolio is indeed underperforming market expectations, but then tell a more reassuring story with more and better data.. “When clients come to you saying, it looks really bad,” says Yang, “you can say, yes, it indeed looks bad right now; here’s how bad. But then you show them slightly longer time horizons, and they can see that things are much less alarming, that the longer-term returns are much closer to what was expected and planned for.”

Yang has found that some advisory firms will stress test their portfolios during a demo and discover that the asset mixes they’ve been recommending to clients are not, and never have been, on any historical efficient frontier. Many of those advisors will quietly never call her again.

Others will use the tool to tweak their asset mixes, and still others have discovered that some of their portfolios, when mapped in risk/return space over different time periods, tended to offer similar returns, even though they looked very different from the outside. So these users would eliminate the redundant portfolio from their model menu.

Finally some advisors are using the current and historical data to show how their alpha-generating or risk mitigation efforts have worked over different

time periods. “One advisory firm has models that provide significant downside protection,” says Yang. “The software lets them show their excellent returns during bear markets, and how that has impacted their clients’ long-term performance.”

Another firm has a strategic model that has consistently outperformed the benchmarks. And there are others that stay humble and keep their clients invested by showing that long-term returns are not greatly affected by market fluctuations. We’re making it easier,” Yang adds, “for advisory firms to tell their story, whatever that may be.”

As a total onboarding solution, Andes lacks only a forms filler that would allow clients to input basic information like names and family names, ages, address, income, expected retirement age—the things that you would normally have to input manually. Yang is working on an additional questionnaire that would gather this basic data directly from the client.

Outlier management

How are advisory firms using Andes with their clients? “We’ve integrated it with Schwab, which is our main custodian,” says Lloyd Easters, chief investment strategist with JarredBunch in Indianapolis, IN. “Andes maps out the performance of each of our client portfolios along the efficient frontier, so we can see how far apart or aligned they are

based on what the market has been doing over a lot of different time periods.”

“When prospects knock on the door,” Easters adds, “we’ll show them a side-by-side comparison of their current portfolio vs. a recommended one, and we can use Andes Wealth to show the statistical data and performance.”

JarredBunch advisors can also graph, in risk/return space, every client portfolio that the firm manages, looking for any outliers. “Then, from a management standpoint, I can ask: why is this person way out there?” says Easters.

He’s constantly checking to make sure all client accounts are allocated appropriately. When they are not, there is usually a reason. “The answer is always: they have a very high risk tolerance, or a lot of legacy assets,” says Easters. “I recently noticed that one client had a highly-appreciated stock position that they didn’t want to sell, so the portfolio’s return was skewed from what our other portfolios were doing.”

Easters likes the Andes risk tolerance instrument and plans to shift to it from the one that JarredBunch is currently using. Finally, his firm is customizing the Andes IPS for the firm’s use, and this longer version is being made available to Andes users (genericized, of course) as an alternative to use in their practices. “Helen is one of the smartest people in our industry,” says Easters. “She’s creating a tool that is going to really make a difference.” ■